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# DOD FINANCIAL MANAGEMENT

## Integrated Approach, Accountability, and Incentives Are Keys to Effective Reform

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# G A O

Accountability \* Integrity \* Reliability

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<b>Abstract</b> Thank you for the opportunity to discuss the status of financial management at the Department of Defense (DOD). Mr. Chairman, I want to commend you for holding this hearing today. As our nation moves into the 21st century, the 107th Congress and the new administration face an array of challenges and opportunities to enhance the performance and assure the accountability of the federal government for the benefit of all Americans. For DOD, changing security threats, increased globalization, and rapid technological advances are prompting fundamental changes in the environment in which it operates. These trends are placing a premium on increasing strategic planning, using integrated approaches, enhancing results-orientation, and ensuring accountability.		
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Mr. Chairman and Members of the Subcommittee:

Thank you for the opportunity to discuss the status of financial management at the Department of Defense (DOD). Mr. Chairman, I want to commend you for holding this hearing today. As our nation moves into the 21st century, the 107th Congress and the new administration face an array of challenges and opportunities to enhance the performance and assure the accountability of the federal government for the benefit of all Americans. For DOD, changing security threats, increased globalization, and rapid technological advances are prompting fundamental changes in the environment in which it operates. These trends are placing a premium on increasing strategic planning, using integrated approaches, enhancing results-orientation, and ensuring accountability.

With DOD spending currently representing about 16 percent of the federal budget—down from about 50 percent in 1962, it is increasingly important that it get the most from every Defense dollar spent. Each Defense dollar that is spent inefficiently is a dollar that is unavailable to meet other departmental priorities, such as weapon system modernization and readiness, or to meet other governmentwide needs. Over the past few years, DOD has made incremental improvements in financial management. However, the results of the department's fiscal year 2000 financial audit are one indicator of the continuing serious and pervasive weaknesses in its financial management systems, operations, and internal controls that have impeded the development of useful, reliable, and timely financial information for day-to-day management and decision-making.

The department's financial management problems are closely tied to its other seven major management challenges—strategic planning, human capital, information technology, acquisition, contract management, support infrastructure, and logistics. An estimated 80 percent of the data needed for sound financial management comes from the department's other business operations, such as acquisitions and logistics. As discussed in our January 2001 reports<sup>1</sup> addressing the major performance and accountability challenges and high-risk areas facing DOD, while our military forces are second to none, this same level of excellence is not evident in many of the business processes that are critical to achieving the department's mission in a reasonably economical, efficient, and effective

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<sup>1</sup>*Major Management Challenges and Program Risks: Department of Defense* (GAO-01-244, January 2001) and *High-Risk Series* (GAO-01-263, January 2001).

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manner. These eight key interrelated areas represent the department's greatest challenge to developing world-class business operations to support its forces.

Today, I will focus on (1) an overview of the long-standing financial management weaknesses facing DOD—as highlighted by the recent results of the fiscal year 2000 financial audit, (2) the underlying causes of DOD's financial management challenges, and (3) key actions necessary to correct DOD's financial management problems as part of a fundamental business process reform.

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## Long-standing Financial Management Weaknesses Continue

We have been reporting on the department's financial management as an area of high risk since 1995.<sup>2</sup> As discussed in our recent report on the results of our review of the fiscal year 2000 Financial Report of the U.S. Government,<sup>3</sup> DOD's financial management deficiencies, taken together, continue to represent the single largest obstacle to achieving an unqualified opinion on the U.S. government's consolidated financial statements. To date, none of the military services or major DOD components have passed the test of an independent financial audit because of pervasive weaknesses in financial management systems, operations, and controls.

These weaknesses not only hamper the department's ability to produce timely and accurate financial management information, but also make the cost of carrying out missions unnecessarily high. Ineffective asset accountability and the lack of effective internal controls continue to adversely affect visibility over its estimated \$1 trillion investment in weapon systems and inventories. Such information is key to meeting military objectives and readiness goals. Further, unreliable cost and budget information related to nearly a reported \$1 trillion of liabilities and about \$347 billion of net costs negatively affects DOD's ability to effectively measure performance, reduce costs, and maintain adequate funds control. As the results of the department's fiscal year 2000 financial

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<sup>2</sup>GAO has designated government operations and programs as "high risk" because of either their greater vulnerabilities to waste, abuse, and mismanagement or major challenges associated with their economy, efficiency, or effectiveness.

<sup>3</sup>*U.S. Government Financial Statements: FY 2000 Reporting Underscores the Need to Accelerate Federal Financial Management Reform* (GAO-01-570T, March 30, 2001).

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audit and other recent auditors' reports demonstrate, DOD continues to confront serious weaknesses in the following areas.

**Budget execution accounting.** The department was unable to reconcile an estimated \$3.5 billion difference between its available fund balances according to its records and Treasury's at the end of fiscal year 2000—similar in concept to individuals reconciling their checkbooks with their bank statements. In addition, the department made frequent adjustments of recorded payments between appropriation accounts, including adjustments to cancelled appropriation accounts<sup>4</sup> of at least \$2.7 billion during fiscal year 2000. In addition, a number of obligations were incorrect or unsupported. For example, auditors found that \$517 million of the \$891 million in recorded Air Force fiscal year 2000 obligations tested were not supported. Further, the department could not fully and accurately account for an estimated \$1.8 billion of transactions that were held in suspense accounts<sup>5</sup> at the end of fiscal year 2000.

The net effect of DOD's problems in this area is that it does not know with certainty the amount of funding it has available. Until the department can effectively reconcile its available fund balances and Treasury's, ensure that payments are posted to the correct appropriation accounts, and post amounts held in suspense accounts to the proper appropriation accounts, the department will have little assurance that reported appropriation balances are correct. Such information is essential for DOD and the Congress to determine if funds are available that could be used to reduce current funding requirements or that could be reprogrammed or transferred to meet other critical program needs.

**Environmental and disposal liabilities.** The amounts of environmental and disposal liabilities the department has reported over the last few years has varied by tens of billions of dollars—from \$34 billion in fiscal year 1998, up to \$80 billion in fiscal year 1999, and down to \$63 billion in fiscal year 2000. However, these reported amounts potentially excluded billions of dollars of future liabilities associated with DOD's non-nuclear weapons; conventional munitions; training ranges; and other property, plant and

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<sup>4</sup>Agencies are required to account for obligated and unobligated balances of their appropriations for 5 years after the expiration of their period of availability. At the end of 5 years, appropriation balances, both obligated and unobligated, are cancelled.

<sup>5</sup>A suspense account is a temporary holding account for problem transactions—for example, those rejected because of system edit controls.

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equipment—such as landfills. For example, we recently reported<sup>6</sup> that while DOD reported a fiscal year 2000 liability of \$14 billion associated with its environmental cleanup of training ranges, other DOD estimates show that this liability could exceed \$100 billion. Obtaining reliable estimates of the department's environmental liability is an important factor for DOD managers and oversight officials to consider with respect to the likely timing of related funding requests and DOD's ability to carry out its environmental cleanup and disposal responsibilities.

**Asset accountability.** DOD has continued to experience problems in properly accounting for and reporting on its weapon systems and support equipment. Material weaknesses continue in the central systems DOD relies on to maintain visibility over assets critical to meeting military objectives and readiness goals. For example, in fiscal year 1999, auditors found that Army's central visibility system excluded information on 56 airplanes, 32 tanks, and 36 Javelin command-launch units. Auditors' fiscal year 2000 financial audit testing showed that previously identified problems in the systems and processes that DOD relied on to account for and control its large investment in weapon systems had not yet been corrected.

In addition, DOD's inability to account for and control its huge investment in inventories has been an area of major concern for many years.<sup>7</sup> For example, auditors' fiscal year 2000 reviews revealed that (1) Army did not perform required physical counts for wholesale munitions with an estimated value of \$14 billion and (2) central accountability and visibility records at four Army test facilities excluded data on about 62,000 missiles, rockets, and other ammunition items that were on hand. In addition, physical counts at the Defense Logistics Agency's 20 distribution depots showed that none of the depots achieved the department's goal of 95 percent inventory record accuracy—with error rates ranging from 6 to 26 percent.

As a result of continuing problems in this area, the department continues to spend more than necessary to procure inventory and at the same time, experience equipment readiness problems because of the lack of key spare parts. For example, we reported that because of long-standing

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<sup>6</sup>*Environmental Liabilities: DOD Training Range Cleanup Cost Estimates Are Likely Understated* (GAO-01-479, April 11, 2001).

<sup>7</sup>GAO-01-263.

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weaknesses in controls over shipments, the department's inventories are at high risk for undetected loss and theft. At the same time, and for a number of years, insufficient spare parts have been recognized as a major contributor to aircraft performing at lower mission capable rates than expected. Our recent reporting<sup>8</sup> disclosed that inaccurate, inconsistent, and missing pricing data for weapon system spare parts undermined military units' ability to buy needed spare parts.

**Net cost information unreliable.** A continuing inability to capture and report the full cost of its programs represents one of the most significant impediments facing the department. DOD does not yet have the systems and processes in place to capture the required cost information from the hundreds of millions of transactions it processes each year. Consequently, while DOD reported \$347 billion in total net costs for its fiscal year 2000 operations, it was unable to support this amount.

The lack of reliable, cost-based information hampers DOD across nearly all its programs and operations. For example, recent reporting highlights the adverse impact the lack of such information has had on the department's studies conducted under Office of Management and Budget (OMB) Circular A-76 and its performance measurement and cost reduction efforts. For example, in December 2000, we reported<sup>9</sup> that our review of DOD functions that were studied over the past 5 years for potential outsourcing under OMB Circular A-76 showed that while DOD reported that savings had occurred as a result of these studies, we could not determine the precise amounts of any such savings because the department lacks actual cost data.

Lacking complete and accurate overall life-cycle cost information for weapon systems impairs DOD and congressional decisionmakers' ability to make fully informed judgments on funding comparable weapon systems. DOD has acknowledged that the lack of a cost accounting system is the single largest impediment to controlling and managing weapon

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<sup>8</sup> *Defense Acquisitions: Prices of Marine Corps Spare Parts Have Increased* (NSIAD-00-123, July 31, 2000), *Defense Acquisitions: Price Trends for Defense Logistics Agency's Weapon System Parts* (GAO-01-22, November 3, 2000), and *Navy Aviation Spare Parts Billing Transaction Issues* (GAO-01-178R, January 11, 2001).

<sup>9</sup> *DOD Competitive Sourcing: Results of A-76 Studies Over the Past 5 Years* (GAO-01-20, December 7, 2000).

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system costs, including the cost of acquiring, managing, and disposing of weapon systems.

In addition, the measures used in the department's reporting under the Government Performance and Results Act (GPRA) often did not address the cost-based efficiency aspect of performance, making it difficult for DOD to fully assess the efficiency of its performance. For example, we reported<sup>10</sup> that while DOD's performance plan for 2001 included 45 unclassified metrics, few metrics contained efficiency measures based on costs.

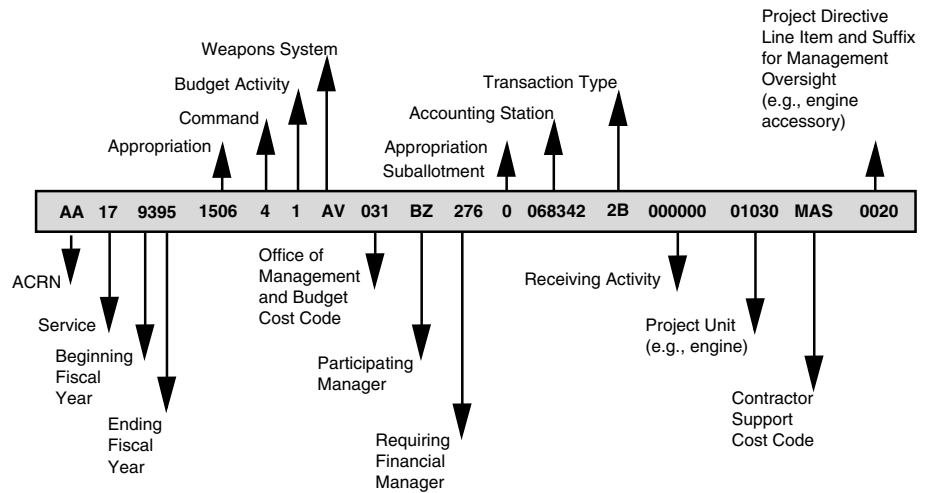
**Financial management systems.** DOD lacks integrated, transaction-driven, double entry accounting systems that are necessary to properly control assets and control costs. DOD has acknowledged that, overall, its reported network of 167 critical financial management systems does not comply with the Federal Financial Management Improvement Act's federal financial management systems requirements.

DOD's transaction processing, using a large network of systems relied on to carry out its financial management operations, is overly complex and error-prone. Each of the military services continue to operate many stand-alone, nonstandard financial processes and systems. As a result, millions of transactions must be manually keyed and rekeyed into the vast number of systems involved in any given DOD business process. To further complicate processing, transactions must be recorded using a coding structure that, as illustrated in the following figure, can exceed 50 digits.

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<sup>10</sup> *Observations on the Department of Defense's Fiscal Year 1999 Performance Report and Fiscal Year 2001 Performance Plan* (GAO/NSIAD-00-188R, June 30, 2000).

**Figure 1: Example of DOD's Accounting Coding**



Source: DOD.

DOD uses such coding—which according to DOD can exceed 75 digits—to accumulate appropriation, budget, and management information for contract payments. In addition, such accounting coding often differs—in terms of type, quantity, and format of data required—by military service and fund type.

As a result, financial accountability is lacking and financial management information available for day-to-day decision-making is poor. Weak systems and controls leave the department vulnerable to fraud and improper payments. For example, DOD continues to overpay contractors. Although the full extent of overpayments is not known, the department has an annual budget for purchases involving contractors of over \$130 billion. In October 2000, we reported<sup>11</sup> that of the \$3.6 billion DOD reported in its fiscal year 1999 financial statements as uncollected debt related to a variety of contract payment problems, at least \$225 million represented improper payments, including duplicate payments, overpayments, and payments for goods not received. Without effective controls over this important area, DOD will continue to risk erroneously

<sup>11</sup> *Financial Management: Billions in Improper Payments Continue to Require Attention* (GAO-01-44, October 27, 2000).

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paying contractors millions of dollars and incur additional, unnecessary costs to collect amounts owed from contractors.

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## Underlying Causes of Financial and Related Business Process Reform Challenges

DOD has initiated a number of departmentwide reform initiatives to improve its financial operations as well as other key business support processes. These initiatives have produced some incremental improvements, but have not resulted in the fundamental reform necessary to resolve these long-standing management challenges.

The underlying causes for the department's inability to resolve its long-standing financial management problems, as well as the other areas of its operations most vulnerable to waste, fraud, abuse, and mismanagement were first identified in our May 1997 testimony.<sup>12</sup> These conditions remain largely unchanged today. Specifically, we believe the underlying reasons for the department's inability to put fundamental reforms of its business operations in place are

- a lack of top-level leadership and management accountability for correcting problems;
- cultural resistance to change, including service parochialism and stovepiped operations;
- a lack of results-oriented goals and performance measures and monitoring; and
- inadequate incentives for seeking change.

**Lack of leadership and accountability.** DOD has not routinely established accountability for performance to specific organizations or individuals that have sufficient authority to accomplish desired goals. For example, under the CFO Act, it is the responsibility of agency CFOs to establish the mission and vision for the agency's future financial management. However, at DOD, the Comptroller—who is by statute the department's CFO—has direct responsibility for only an estimated 20 percent of the data relied on to carry out the department's financial management operations. The department has learned through its efforts to meet the Year 2000 computing challenge that to be successful, major improvement initiatives must have the direct, active support and involvement of the Secretary and Deputy Secretary of Defense. Such top-

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<sup>12</sup> *DOD High-Risk Areas: Eliminating Underlying Causes Will Avoid Billions of Dollars in Waste* (GAO/T-NSIAD/AIMD-97-143, May 1, 1997).

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level support helps guarantee that daily activities throughout the department remain focused on achieving shared, agency-wide outcomes.

DOD experience has suggested that top management has not had a proactive, consistent, and continuing role in building capacity, integrating daily operations for achieving performance goals, and in creating incentives. Sustaining top management commitment to performance goals is a particular challenge for DOD. In the past, a turnover rate among the department's top political appointees of 1.7 years hindered long-term planning and follow-through.

**Cultural resistance and parochialism.** Cultural resistance to change and service parochialism have also played a significant role in impeding DOD management reforms. DOD has acknowledged that it confronts decades-old problems deeply grounded in the bureaucratic history and operating practices of a complex, multifaceted organization, and that many of these practices were developed piecemeal and evolved to accommodate different organizations, each with its own policies and procedures.

For example, as discussed in our July 2000 report,<sup>13</sup> the department has encountered resistance to developing departmentwide solutions under the Secretary's broad-based Defense Reform Initiative (DRI).<sup>14</sup> The department established a Defense Management Council—including high-level representatives from each of the military services—which was intended to serve as the "board of directors" to help break down organizational stovepipes and overcome cultural resistance to changes called for under DRI. However, we found that the council's effectiveness was impaired because members were not able to put their individual military services' or DOD agencies' interests aside to focus on departmentwide approaches to long-standing problems.

We have also seen an inability to put aside parochial views and cultural resistance to change impeding reforms in the department's weapon system acquisition and inventory management areas. For example, as we recently

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<sup>13</sup> *Defense Management: Actions Needed to Sustain Reform Initiatives and Achieve Greater Results* (GAO/NSIAD-00-72, July 25, 2000).

<sup>14</sup> Announced by the Secretary of Defense in 1997, DRI represents a set of actions aimed at reforming the department's major business processes and support operations.

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reported,<sup>15</sup> while the individual military services conduct considerable analyses justifying major acquisitions, these analyses can be narrowly focused and do not consider joint acquisitions with the other services. In the inventory management area, DOD's culture has supported buying and storing multiple layers of inventory rather than managing with just the amount of stock needed.

**Unclear goals and performance measures.** Further, DOD's reform efforts have been handicapped by the lack of clear, hierarchically linked goals and performance measures. As a result, DOD managers lack straightforward road maps showing how their work contributes to attaining DOD's strategic goals, and they risk operating autonomously rather than collectively. In some cases, DOD had not yet developed appropriate strategic goals, and in other cases, its strategic goals and objectives were not linked to those of the military services and defense agencies.

As part of our assessment of *DOD's Fiscal Year 1999 Performance Report*, we reported<sup>16</sup> that it did not include goals or measures for addressing its contracting challenge, and it was not clear whether the department had achieved identified key program outcomes. The department's 1999 performance report did not provide any information on whether DOD is achieving any reduction in the important area of erroneous payments to contractors nor did it provide any cost-based measures for whether the department had achieved its desired outcome of putting in place a more efficient and cost-effective infrastructure and associated operating procedures.

Many of the department's business processes in operation today are mired in old, inefficient processes and systems, many of which are based on 1950s and 1960s technology. The department faces a formidable challenge in responding to technological advances that are changing traditional approaches to business management as it moves to modernize its systems. For fiscal year 2000, DOD reported total information technology investments of over \$21 billion supporting a wide range of military operations as well as its business functions, including an estimated \$7.6 billion in major information system projects. While DOD plans to

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<sup>15</sup> *Major Management Challenges and Program Risks: Department of Defense* (GAO-01-244, January 2001).

<sup>16</sup> [GAO/NSIAD-00-188R](#), June 30, 2000.

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invest billions of dollars in modernizing its financial management and other business support systems, it does not yet have an overall blueprint—or enterprise architecture—in place to guide and direct these investments.

**Lack of incentives for change.** The final underlying cause of the department's inability to carry out needed fundamental reform is the lack of incentives for making more than incremental change to existing "business as usual" processes, systems, and structures. Traditionally, DOD has focused on justifying its need for more funding rather than on the outcomes its programs produced. DOD generally measures its performance by the amount of money spent, people employed, or number of tasks completed. Incentives for DOD decisionmakers to implement changed behavior have been minimal or nonexistent.

This underlying problem has perhaps been most evident in the department's acquisition area. In DOD's culture, the success of a manager's career has depended more on moving programs and operations through the DOD process rather than on achieving better program outcomes. The fact that a given program may have cost more than estimated, took longer to complete, and did not generate results or perform as promised is secondary to fielding a new program. To effect real change, actions are needed to (1) break down parochialism and reward behaviors that meet DOD-wide and congressional goals, (2) develop incentives that motivate decisionmakers to initiate and implement efforts that are consistent with better program outcomes, and (3) facilitate a congressional focus on results-oriented management, particularly with respect to resource allocation decisions.

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## Keys to Fundamental DOD Business Process Reform

The new Secretary of Defense has stated that he intends to include financial management reform among his top priorities. The Secretary faces a monumental task in putting in place such a fundamental reform. The size and complexity of DOD's operations are unparalleled. DOD is not only responsible for an estimated \$1 trillion in assets and liabilities, but also for supporting personnel on an estimated 500 bases in 137 countries and territories throughout the world. It has also estimated that it makes \$24 billion in monthly disbursements, and that in a given fiscal year, the department may have as many as 500 or more active appropriations. Given the unparalleled nature of DOD's operations, combined with its deeply entrenched financial management weaknesses, it will not be possible to fully resolve these problems overnight. Changing how DOD carries out its financial management operations is going to be tough work.

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Going forward, various approaches could be used to address the underlying causes of DOD's financial management challenges. But, consistent with our previous testimony before your subcommittee, as well as the results of our survey of world-class financial management organizations and other recent reviews,<sup>17</sup> there are several elements that will be key to any successful approach to reform

- address the department's financial management challenges as part of a comprehensive, integrated, DOD-wide business process reform;
- provide for active leadership by the Secretary of Defense and resource control to implement needed financial management reforms;
- establish clear lines of responsibility, authority, and accountability for such reform tied to the Secretary;
- incorporate results-oriented performance measures tied to financial management reforms;
- provide appropriate incentives or consequences for action or inaction;
- establish an enterprisewide architecture to guide and direct financial management modernization investments; and
- ensure effective oversight and monitoring.

**Integrated business process reform strategy.** As we have reported in the past,<sup>18</sup> establishing the right goal is essential for success. Central to effectively addressing DOD's financial management problems will be the recognition that they cannot be addressed in an isolated or piecemeal fashion separate from the other major management challenges and high-risk areas facing the department.<sup>19</sup> Successfully reengineering the department's processes supporting its business operations will be critical if DOD is to effectively address deep-rooted organizational emphasis on maintaining "business as usual" across the department.

Financial management is a crosscutting issue that affects virtually all of DOD's business processes. For example, improving its financial

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<sup>17</sup> *Department of Defense: Progress in Financial Management Reform* (GAO/T-AIMD/NSIAD-00-163, May 9, 2001) and *Executive Guide: Creating Value Through World-class Financial Management* (GAO/AIMD-00-134, April 2000).

<sup>18</sup> GAO/T-AIMD/NSIAD-00-163.

<sup>19</sup> As discussed previously, the eight interrelated areas that represent the greatest challenge to DOD developing world-class business operations supporting its forces are: strategic planning, human capital, financial management, information technology, acquisition, contract management, support infrastructure, and logistics.

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management operations so that they can produce useful, reliable, and timely cost information will be essential if the department is to effectively measure its progress toward achieving many key outcomes and goals across virtually the entire spectrum of DOD's business operations. At the same time, the department's financial management problems—and, most importantly, the keys to their resolution—are deeply rooted in and dependent upon developing solutions to a wide variety of management problems across DOD's various organizations and business functions. The department has reported that an estimated 80 percent of the data needed for sound financial management comes from the department's other business operations, such as its acquisition and logistics communities. DOD's vast array of costly, non-integrated, duplicate, inefficient financial management systems is reflective of the lack of an enterprise wide, integrated approach to addressing its management challenges. DOD has acknowledged that one of the reasons for the lack of clarity in its reporting under the GPRA was that most of the program outcomes the department is striving to achieve are interrelated.

**Active leadership and resource control.** The department's successful Year 2000 effort illustrated and our survey of leading financial management organizations<sup>20</sup> captured the importance of strong leadership from top management. As we have stated many times before, strong, sustained executive leadership is critical to changing a deeply rooted corporate culture—such as the existing “business as usual” culture at DOD—and successfully implementing financial management reform. The personal, active involvement of the Deputy Secretary of Defense played an important role in building entity wide support for the department's Year 2000 initiatives. Given the long-standing and deeply entrenched nature of the department's financial management problems combined with the numerous competing DOD organizations, each operating with varying and often parochial views and incentives, such visible, sustained top-level leadership will be critical.

**Clear lines of responsibility and accountability.** Establishing clear lines of responsibility, decision-making authority, and resource control for actions across the department tied to the Secretary will also be a key to reform. As we reported<sup>21</sup> with respect to the department's implementation

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<sup>20</sup> *Executive Guide: Creating Value Through World-class Financial Management* (GAO/AIMD-00-134, Apr. 2000).

<sup>21</sup> GAO/NSIAD-00-72.

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of its DRI, such an accountability structure should emanate from the highest levels and include the secretaries of each of the military services as well as heads of the department's various business areas.

**Results-oriented performance.** As discussed in our report on DOD's major performance and accountability challenges,<sup>22</sup> establishing a results-orientation will be another key element of any approach to reform. Such an orientation should draw upon results that could be achieved through commercial best practices, including outsourcing and shared servicing concepts. Personnel throughout the department must share the common goal of establishing financial management operations that not only produce financial statements that can withstand the test of an audit but, more importantly, also routinely generate useful, reliable, and timely financial information for day-to-day management purposes.

In addition, we have previously testified<sup>23</sup> that DOD's financial management improvement efforts should be measured against an overall goal of effectively supporting DOD's basic business processes, including appropriately considering related business process system interrelationships, rather than determining system-by-system compliance. Such a results-oriented focus is also consistent with an important lesson learned from the department's Year 2000 experience. DOD's initial Year 2000 focus was geared toward ensuring compliance on a system-by-system basis and did not appropriately consider the interrelationship of systems and business areas across the department. It was not until the department shifted to a core mission and function review approach that it was able to achieve the desired result—greatly reducing its Year 2000 risk.

**Incentives and consequences.** Another key to breaking down parochial interests and stovepiped approaches that have plagued previous reform efforts will be establishing mechanisms to reward organizations and individuals for behaviors that comply with DOD-wide and congressional goals. Such mechanisms should provide appropriate incentives and penalties to motivate decisionmakers to initiate and implement efforts that result in fundamentally reformed financial management operations.

**Enterprise architecture.** Establishing an enterprise wide financial management architecture will be essential for the department to

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<sup>22</sup>GAO-01-244.

<sup>23</sup>GAO/T-AIMD/NSIAD-00-163.

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effectively manage its large, complex system modernization effort now underway. As we testified last year,<sup>24</sup> the Clinger-Cohen Act requires agencies to develop and maintain an integrated system architecture. Such an architecture can help ensure that the department invests only in integrated, enterprise wide business system solutions, and conversely, will help move resources away from non-value added legacy business systems and nonintegrated business system development efforts. In addition, without an architecture, DOD runs the serious risk that its system efforts will result in perpetuating the existing system environment that suffers from systems duplication, limited interoperability, and unnecessarily costly operations and maintenance. In a soon to be issued report, we point out that DOD lacks a financial management enterprise architecture to guide and constrain the billions of dollars it plans to spend to modernize its financial management operations and systems.

**Monitoring and oversight.** Ensuring effective monitoring and oversight of progress will also be a key to bringing about effective implementation of the department's financial management and related business process reform. We have previously testified<sup>25</sup> that periodic reporting of status information to OMB, the Congress, and the audit community was another key lesson learned from the department's successful effort to address its Year 2000 challenge. Finally, this Subcommittee's annual oversight hearings, as well the active interest and involvement of other cognizant Defense committees, will continue to be key to effectively achieving and sustaining DOD's financial management and related business process reform milestones and goals.

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In closing, while DOD has made incremental improvement, it has a long way to go to address its long-standing, serious financial management weaknesses as part of a comprehensive, integrated reform of the department's business support operations. Such an overhaul must include not only DOD's financial management and other management challenges, but also its high-risk areas of information technology and human capital management. Personnel throughout the department must share the common goal of reforming the department's business support structure.

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<sup>24</sup> [GAO/T-AIMD/NSIAD-00-163](#).

<sup>25</sup> [GAO-01-244](#).

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The transition to modern performance management and, along with it, to strategic human capital and information technology management, will require a cultural transformation throughout the department that will take time. DOD will need to be more partnerial, results oriented, integrated, and externally focused in the future. Without reengineering, DOD will have little chance of radically improving its existing cumbersome and bureaucratic processes. Such a fundamental reform will require sustained commitment from the highest levels of DOD leadership and changes throughout all levels of the department as well as vigorous congressional oversight. We stand ready to help the Congress and the administration put in place world-class business operations in support of our forces by providing professional, objective, and constructive assistance.

Mr. Chairman, this concludes my statement. I will be happy to respond to any questions you or other members of the Subcommittee may have.